A White House proposal for a new federal agency to police mortgages and credit cards has triggered a clash among House Democrats and threatens to complicate the Obama administration's effort to overhaul financial-market rules.

Democrats are split over whether the proposal should allow states to trump federal regulations and enforce their own, often tougher consumer rules against national banks, such as Bank of America Corp., J.P. Morgan Chase & Co. and Wells Fargo & Co. This would permit states to bar certain fees and late charges otherwise allowed by federal regulators.

WSJ's Damian Paletta reports a key question dividing Democrats in Congress is who should have more power to protect consumers -- the states or the federal government.

The issue has become a flashpoint in the debate and a problem for divided Democrats, who are trying to marshal support for a White House proposal struggling for momentum. And it comes as Treasury Department officials plan their own push this month to revive interest in their overhaul effort. They fear a drawn-out debate could bog down the process. Treasury Secretary Timothy Geithner is holding a series of meetings with Democrats to bolster support.

The White House proposal would create a new Consumer Financial Protection Agency with the power to write and enforce rules against a range of products. States would be allowed to write stricter rules than the CFPA, overturning existing policies under which national banks typically are immune from state regulation.

The issue could come to a head next week. House Financial Services Committee Chairman Barney Frank (D., Mass.) is expected to hold a vote in his committee to create the new agency. Rep. Melissa Bean (D., Ill.) is preparing an amendment that would prevent states from enforcing tougher standards against national banks than the federal entity's. Her amendment would allow state attorneys general to file civil charges against banks that violate federal rules, as long as the state officials handed the cases over to federal officials later.

Ms. Bean says the White House plan would force financial institutions to follow more than 50 different sets of rules, potentially driving up the cost of credit. "This is longstanding precedent that those institutions with a national charter have a single set of rules to comply with," she said.

Opponents of the Bean amendment, such as Rep. Brad Miller (D., N.C.), say states need more clout in case federal regulators don't keep banks in check. He said he and other Democrats would vote against the entire bill if Ms. Bean's amendment was accepted.

The fight has created a minefield for the administration. Treasury officials aren't counting on a lot of Republican votes for the White House plan, which means a splintering of Democrats could threaten the bill.

"There's a number of fissures and fault lines out there on the Democratic side," said Rep. John Campbell (R., Calif.), a member of Mr. Frank's committee. He predicted all Republicans on the panel would vote for Ms. Bean's amendment.

A Bank of America spokesman said the company was supportive of "enhanced consumer protections" but remained "concerned about the impact on efficiency if each state had different rules and regulations for bank products."

Consumer groups say Ms. Bean's amendment could weaken consumer protection because federal rules could be eased in several years once the financial crisis recedes. Generally, states have tougher consumer rules than federal agencies, although not all of them enforce the rules aggressively.

Treasury officials haven't backed down from their proposal.

"If a state wants to provide for its citizens' stronger consumer protections, it ought to be able to do so," Deputy Treasury Secretary Neal Wolin told reporters recently.

Mr. Frank has long called for more state enforcement power but is trying to appease both sides. "We're still having discussions with our members on the issue," a spokesman for Mr. Frank said.